No. 17361

In the United States Court of Appeals for the Ninth Circuit

STANDARD LUMBER CO., formerly
PILOT ROCK LUMBER CO., PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

On Petition for Review of the Decision of the Tax Court of the United States

BRIEF FOR THE RESPONDENT

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CITATIONS

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OPINION BELOW

The opinion of the Tax Court (R. 9-21) is reported at 35 T.C. 192.

JURISDICTION

This petition for review (R. 23-26) involves federal income taxes for the taxable year 1954. On September 11, 1958, the Commissioner of Internal Revenue mailed to the taxpayer notice of a deficiency for the year 1954 in the total amount of $255,939.96.

(R. 10, 32.) Within ninety days thereafter the taxpayer filed a petition with the Tax Court for a redetermination of that deficiency under the provisions of Section 6213 of the Internal Revenue Code of 1954.[1] The decision of the Tax Court was entered December 27, 1960. (R. 22.) The case is brought to this Court by a petition for review filed March 23, 1960. (R. 23-26.) Jurisdiction is conferred on this Court by Section 7482 of the Internal Revenue Code of 1954.

QUESTION PRESENTED

During 1954 the taxpayer owned approximately 62 per cent of the outstanding common stock of a second corporation, trustees under a voting trust agreement owned approximately 25 per cent, and all others owned approximately 13 per cent. The voting trust agreement was for a twenty-year period and was valid when executed in 1952. A subsequent state statute, effective December 31, 1953, provided that a voting trust can be created for a period not to exceed ten years.

The question is whether during 1954 the taxpayer owned directly stock possessing at least 80 per cent of the voting power of all classes of stock of the second corporation so as to entitle it to file a consoli-

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[1] The administrative records of the Internal Revenue Service indicate that taxpayer's petition was received by the Tax Court on December 12, 1958, but was postmarked December 8, 1958, and therefore should be deemed filed within ninety days after September 11, 1958, under Section 7502 of the Internal Revenue Code of 1954.

dated return with that company under Section 1504 (a) (2) of the Internal Revenue Code of 1954.

STATUTES INVOLVED

The pertinent portions of the statutes involved are set forth in the Appendix, *infra*.

STATEMENT

The facts, as found by the Tax Court (R. 10-21) and developed by stipulation (R. 27-33), may be summarized as follows:

The taxpayer, Standard Lumber Company, is a dissolved and liquidated corporation which was organized under the laws of the State of Oregon and had its principal office at Pilot Rock, Oregon. Liquidation of the taxpayer was completed on June 30, 1956. Oregon Fibre Products, Inc., hereinafter referred to as Products, also was incorporated under the laws of the State of Oregon and had its principal office at Pilot Rock. The taxpayer and Products maintained their books and reported income on an accrual method of accounting by calendar years, and timely filed a consolidated income tax return for 1954. (R. 11.)

During 1954 Products had two classes of authorized stock, common and preferred. The preferred stock did not possess voting rights and was limited and preferred as to dividends. During 1954 the taxpayer held approximately 62 per cent of Products' outstanding common stock, trustees under a voting

trust agreement held approximately 25 per cent, and all others held approximately 13 per cent.[2] (R. 11.)

The voting trust agreement under which the trustees held approximately 25 per cent of stock of Pr... ucts outstanding during 1954 was created on November 3, 1952, and was terminated by consent of all parties thereto by an agreement dated January 1, 1955. The voting trust agreement empowered the trustees to vote all the shares of Products held under the agreement. It further provided that the trust agreement should continue for 20 years from its date. (R. 11.)[3]

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[2] At all times during 1954 there were issued and outstanding no more than 120,000 shares of the common stock of Products. Throughout 1954 taxpayer owned 74,000 of those shares and 30,000 shares were held in the names of the voting trustees. All other individuals held 14,900 shares on January 1, 1954, and 16,000 shares on December 31, 1954. (R. 28-29.) The common stock held by the voting trustees in 1954 was for the benefit of and for shares as follows (R. 29):

Pilot Rock Lumber Co. (taxpayer's former corporate name)	2,000
Harvey Gunderson	6,000
Carver Investment Company	22,000
	30,000

[3] The voting trust agreement provided (R. 46) that it might be terminated at any time by the execution and acknowledgment by all the trustees of a "deed of termination" and that prior to termination the trustees might "in their discretion by written statement release a portion of the common stock" held under the agreement. The agreement further provided (R. 46):

> Within sixty days after the termination of this agreement the Trustees shall deliver to the registered holders of all voting trust certificates, certificates for the num-

Section 57.175 of the Oregon Revised Statutes, a part of the Oregon Business Corporation Act which was passed during the 1953 session of the Oregon legislature and became effective December 31, 1953, provides that a voting trust can be created for a period not to exceed 10 years. (R. 11-12.)

The Commissioner determined deficiencies in taxpayer's income tax for 1954 on the ground that it was not entitled to file a consolidated return with Products for 1954. (R. 16.) In deficiency proceedings the Tax Court held that the voting trust in issue was valid under Oregon law when executed, that Section 57.175 of the Oregon Business Corporation Act was not intended to operate retrospectively and did not invalidate the pre-existing trust or suspend the voting rights of the shares of Products held in trust, and, therefore, that during 1954 taxpayer did not own stock in Products possessing 80 per cent of the voting power so as to file a consolidated return with Products under the criteria of Section 1504(a)(2) of the Internal Revenue Code of 1954. (R. 17-19.) Accordingly, the Tax Court sustained the Commissioner's determination of deficiencies in the amount of $208,092.16 for 1954.[4]

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ber of shares of common stock represented by the voting trust certificates, upon surrender thereof, properly endorsed.

[4] The Tax Court also held that interest in the amount of $92,015 on debentures issued by Products and held by taxpayer was not properly includible in taxpayer's income for 1954 since certain contingencies qualified the taxpayer's right to receipt of the interest. (R. 19-22.) The Commis-

SUMMARY OF ARGUMENT

Under Sections 1501 and 1504 of the Internal Revenue Code of 1954 consolidated income tax returns may be filed only by certain chains of corporations in which the common parent "owns directly stock possessing at least 80 percent of the voting power of all classes of stock and at least 80 per cent of each class of the nonvoting stock" of an includible corporation. The Tax Court correctly held that taxpayer failed to meet the statutory requirement, and therefore could not avail itself of the privilege of filing a consolidated return. During 1954 taxpayer owned 74,000 shares of the common stock of Products, and there were between 118,900 and 120,000 common shares outstanding. A voting trust created in 1952 owned 30,000 shares, of which 2,000 were held for the benefit of taxpayer. Taxpayer thus owned approximately 62 per cent of Products' common stock, which was less than the amount required to entitle it to file a consolidated return with that company.

Taxpayer's contention that the voting trust as to 30,000 shares of Products' common stock was invalid under a 1953 Oregon statute limiting the duration of voting trusts, and that the trusteed stock therefore was deprived of voting power, is without merit. The

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sioner has not appealed from this portion of the decision.

All issues with respect to the taxable year 1955 were settled by stipulation. Accordingly, the Tax Court sustained the Commissioner's determination of deficiencies in income tax in the amount of $180,397.47 for 1955, and no question concerning the taxable year 1955 is in issue or review. (R. 4, 10.)

trust in question was created prior to the enactment of the Oregon statute, and as pointed out by the Tax Court, was not retrospectively invalidated by that legislation.

Even assuming that the voting trust had been terminated by the Oregon statute, it still would not follow, as taxpayer also assumes, that the voting rights inhering in the trusteed shares disappeared. On the contrary, under the terms of the trust agreement, the trustees were required upon its termination to distribute the shares to the beneficial owners, who could then exercise the voting rights. Since the voting rights which attached to the trusteed shares were exercisable *either* by the trustees or the beneficial owners—irrespective of whether (as taxpayer claims) the voting trust agreement was rendered invalid by the Oregon statute—there is no basis for taxpayer's contention that the rights must be disregarded for purposes of applying Code Section 1504 (a) (2).

Furthermore, taxpayer's entire argument rests upon the unwarranted premise that a dispute as to the ownership of outstanding shares of stock is tantamount to no ownership at all, i.e. non-existence of the stock, for purposes of applying Code Section 1504 (a) (2). As a condition precedent to the privilege of filing a consolidated return that section explicitly requires that the parent corporation own directly (1) stock possessing at least 80 per cent of voting power of the voting stock, plus (2) 80 per cent of each class of nonvoting stock. Under taxpayer's novel theory, any dispute as to ownership of any issued and outstanding shares of stock (voting or nonvoting) would

require disregard of those shares for purposes of determining whether the parent corporation owns the requisite percentage of both the voting and nonvoting stock. Clearly a dispute as to ownership of nonvoting shares would not operate to eliminate them from the total number of issued and outstanding shares for purposes of computing the percentage of nonvoting shares owned by the parent. *A fortiori*, a dispute as to who may exercise the voting rights with respect to outstanding voting stock cannot serve to eliminate such voting stock from the computation formula.

What is more, even assuming *arguendo* that the 30,000 shares in the voting trust are to be viewed as if the voting rights which attached to them were "suspended", and hence to be treated as nonvoting shares, as taxpayer asserts, taxpayer still could not prevail. For under its own reasoning such shares must then be classified as nonvoting shares, and taxpayer admittedly was the beneficial owner of 2,000 of such shares, or far less than the required 80 per cent of nonvoting stock.

ARGUMENT

Taxpayer Did Not Own Stock Possessing 80 Per Cent of the Voting Power of the Common Stock of Products and Hence Was Not Entitled To File a Consolidated Return With Products for 1954, Regardless of Whether the Voting Trust As To 30,000 of Products' Common Shares Was Valid or Invalid During That Year

Section 1501 of the Internal Revenue Code of 1954 (Appendix, *infra*) provides that, subject to certain

limitations, an "affiliated group of corporations shall * * * have the privilege of making a consolidated return" with respect to income taxes. An "affiliated group is defined in Section 1504 (Appendix, *infra*) as including only certain chains of corporations in which the common parent "owns directly stock possessing at least 80 percent of the voting power of all classes of stock and at least 80 percent of each class of the nonvoting stock * * *."

Throughout 1954 there were between 118,900 and 120,000 shares of the common stock of Products outstanding. Taxpayer owned 74,000 shares or approximately 62 per cent of this stock. A voting trust owned 30,000 shares of Products' common stock, 2,000 shares for the benefit of taxpayer. (R. 11, 16, 28-29.) Taxpayer admits (Br. 9) that during 1954 it owned less than 80 per cent of the outstanding shares of Products' common stock, and taxpayer does not claim that any of the shares were entitled to more than one vote.[5]

Taxpayer contends (Br. 5-17) that the voting trust was invalid or of doubtful validity under Oregon law, that the 30,000 shares of Products' common stock held in trust were deprived of voting rights, and that taxpayer's 74,000 shares, though less than 80 per cent of the outstanding 120,000 shares of com-

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[5] There were 5,000 shares of the preferred stock of Products outstanding at all times during 1954. The preferred stock does not possess voting rights and is limited and preferred as to dividends. (R. 28.) Section 1504 of the 1954 Code expressly provides that such preferred stock is not "stock" within the meaning of that section.

mon stock, possessed 80 per cent of the "voting power" of Products' common stock during 1954. On the facts of this case there is no merit in these contentions. Taxpayer did not own stock possessing 80 per cent of the voting power of Products' common stock in 1954 and consequently did not satisfy the requirements of Code Sections 1501 and 1504 for the privilege of filing a consolidated return with Products for 1954.[6]

A. ***The 1952 voting trust as to 30,000 shares of Products' common stock was valid throughout 1954, and the voting power of the trusteed shares was unimpaired by Oregon legislation enacted in 1953***

The Tax Court correctly held (R. 19) that during 1954 the voting trust as to 30,000 shares of common stock of Products was not invalidated. The trust was created by agreement on November 3, 1952, for a period of twenty years, unless sooner terminated. (R. 11, 29, 34, 46.) Prior to the execution of the agreement the validity of voting trusts or pooling agreements had been recognized by the Oregon courts. *Curtze* v. *Iron Dyke Mining Co.*, 46 Or. 601, 81 Pac. 851; *In re Will of Pittock*, 102 Or. 159, 199

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[6] Taxpayer's claim (Br. 9) that it should be considered to have possessed 80 per cent of the voting power of Products' common stock during 1954 because of an alleged "pall of invalidity" over the voting trust is particularly inappropriate as a ground for claiming the "privilege" of filing a consolidated return. See *Commissioner* v. *Manus Muller & Co.*, 79 F. 2d 19, 20, certiorari denied, 296 U.S. 657 where Judge Learned Hand stated that " * * * affiliation is a privilege in any case, akin to an exemption, and doubts go against the taxpayer."

Pac. 633; *Smith* v. *Bramwell*, 146 Or. 611, 31 P. 2d 647. Accordingly, as the Tax Court held (R. 17), the voting trust in issue was valid when executed.

There is no merit in taxpayer's contention that the voting trust was thereafter rendered invalid by Section 57.175 of the Oregon Revised Statutes (Appendix, *infra*), effective December 31, 1953. That Section provides:

> *Voting trust.* Any number of shareholders of a corporation may create a voting trust for the purpose of conferring upon a trustee or trustees the right to vote or otherwise represent their shares, for a period of not to exceed 10 years, by entering into a written voting trust agreement specifying the terms and conditions of the voting trust, by depositing a counterpart of the agreement with the corporation at its registered office, and by transferring their shares to such trustee or trustees for the purposes of the agreement. * * *

On its face the terminology of Section 57.175 is permissive and does not render pre-existing voting trusts void or voidable. Under Oregon law legislation is interpreted as prospective in operation unless a retrospective application clearly is indicated by the terms of the statute. *Hartley* v. *Utah Const. Co.*, 106 F. 2d 953 (C.A. 9th).[7] Statutes similar to Sec-

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[7] In the *Hartley* case, 106 F. 2d 953, 955, this Court stated:

> The rule in Oregon is:
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> "* * * no act will be held to have a retrospective effect, unless the intention in that respect is clearly

tion 57.175 of the Oregon Revised Statutes have also been interpreted in other jurisdictions as applying only prospectively. See 5A Fletcher, Cyclopedia Corporations (Perm. ed., 1952 Rev.), Sec. 2080.1:

> The statutes usually limit * * * duration [of voting trusts] to an arbitrary period, commonly 10 years, and are held to be prospective in operation, applying only to agreements entered into after their effective date.

For example, in *Wolf* v. *Roosevelt*, 290 N.Y. 400, 402, 49 N.E. 2d 502, the New York Court of Appeals gave only prospective effect to a statute which provided: "No agreement appointing trustees to vote the stock of any corporation * * * shall be valid for a longer term than five years * * *." In rejecting the argument that this statute limited the duration of pre-existing voting trusts, the Court of Appeals stated (290 N.Y. 400, 402, 403, 49 N.E. 2d 502, 503):

> * * * a statute restricting the power of individuals to create or define their rights should not be construed in a manner which would affect existing agreements unless the Legislature so provided in express terms or by plain implication. * * * The language of the statute is at least

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apparent in the statute itself. On the contrary, if it is fairly possible to restrain the operation of the statute so as to be prospective, that course will be adopted by the courts. * * *" *Libby* v. *Southern Pac. Co.*, 109 Or. 449, 452, 219 P. 604, 605, 220 P. 1017.

See also *Hoffart* v. *Lindquist & Paget Mortg. Co.*, 182 Or. 611, 620, 189 P. 2d 592, 596.

> inept if the Legislature intended that it should retroactively restrict the power of stockholders to enter into voting trust agreements.
>
> * * * If the statute is intended to apply to agreements already made those who entered into the agreement would be bound by limitations to which they did not agree, although they might never have consented to the plan of reorganization or the voting trust agreement if the agreement had been limited to five years from June, 1936.[8]

See also *Western Pac. R. Corp.* v. *Baldwin*, 89 F. 2d 269 (C.A. 8th), applying these principles of statutory construction and holding that provisions of Delaware law limiting the duration of voting trusts were inapplicable to pre-existing trusts. The same reasoning is applicable to the present case and supports the Tax Court's conclusion that the Oregon statute did not invalidate voting trusts entered into prior to its effective date, December 31, 1953.[9]

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[8] In *Wolf* v. *Roosevelt, supra,* the court rejected the suggestion that by implication the New York statute limited the duration of voting trusts to five years after its enactment. In the present case the taxpayer makes the more extreme contention that the voting trust became invalid on the effective date of the statute limiting its duration. *A fortiori,* this position is inconsistent with *Wolf* v. *Roosevelt, supra.* The voting trust involved in the instant case would be valid during 1954 even if retrospectively limited in duration to ten years from its inception or from the effective date of the Oregon voting trust statute.

[9] In the present case the taxpayer's assertion that Section 57.175 should be applied retroactively to suspend the voting power of shares held by previously existing non-complying trusts would have practical results which the legislature un-

Furthermore, Section 57.799 of the Oregon Revised Statutes (Appendix, *infra*), expressly provides that no right, liability or penalty created under the prior Act should be affected by its repeal, thus indicating that the legislature intended only prospective operation of the new statute. This general intention is not inconsistent with the statement in Section 57.796, (Appendix, *infra*), relied upon by taxpayer (Br. 6-7), that "The provisions of the Oregon Business Corporation Act shall apply * * * to all existing corporations organized under any general Act of this state." Both general expressions of legislative intention may be observed by the prospective application of the new statute to existing corporations. Thus the terms of the statute, applicable authority and principles of statutory construction, and the indicia of legislative intention all demonstrate that Section 57.175 applies only prospectively and did not invalidate the pre-existing trust as to 30,000 shares of Products' common stock during 1954.

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doubtedly did not intend. Taxpayer suggests (Br. 14) that if the majority of the voting stock of a corporation were held by a trust such as that in issue, control of the corporation and all its assets would pass to a minority interest, however small, until such time as the trust was terminated by agreement among all parties or by specific judicial decree. It does not appear likely that the legislature intended that Section 57.175, limiting the duration of voting trusts, should be applied retrospectively to create any such possible distortion of the control and management of corporations.

B. ***Regardless of the validity of the voting trust, taxpayer did not satisfy the Internal Revenue Code requirements of stock ownership for the privilege of filing a consolidated return with Products for 1954***

Even if the pre-existing voting trust were deemed terminated by reason of the enactment of the 1953 Oregon statute, there would have been no impairment of the voting rights of the trusteed shares.

To begin with, the trust agreement specifically provides (R. 46):

> 11. Term Of Agreement And Distribution of Common Stock Upon Termination. * * * After common stock has been deposited under this agreement such common stock cannot be withdrawn until this agreement is terminated unless the Trustees in their discretion by written statement release a portion of the common stock held hereunder * * *.
>
> Within sixty days after the termination of this agreement the Trustees shall deliver to the registered holders of all voting trust certificates, certificates for the number of shares of common stock represented by the voting trust certificates, upon surrender thereof, properly endorsed.

If the voting trust had been terminated by operation of law, the trustees would have been obligated to distribute the trusteed common stock of Products to the beneficial owners and the voting rights of the stock would not have been destroyed even temporarily.[10]

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[10] In the event of such a distribution, taxpayer would have held 2,000 trusteed shares in addition to its 74,000 shares, still less than 80 per cent of the 120,000 outstanding common shares.

Furthermore, and again assuming *arguendo* that the voting trust was rendered invalid by the 1953 Oregon statute, there are additional and alternative reasons for sustaining the decision below.

Under Section 1504 of the 1954 Code, to file a consolidated return a parent corporation must own directly "stock possessing at least 80 percent of the voting power of all classes of stock and at least 80 percent of each class of the nonvoting stock" of a subsidiary. The term "stock" does not include nonvoting preferred stock. Section 1504 imposes no requirements with respect to the ownership of stock of the subsidiary which is held by persons other than the parent corporation.

In essence, the taxpayer's contention is that the amount of Products' voting stock which Section 1504 requires that it own to file a consolidated return should be reduced because of alleged doubt as to the ownership of some shares admittedly not owned by taxpayer. Applied as a general proposition, taxpayer's interpretation of Section 1504(a)(2) would mean that any dispute as to ownership of any issued and outstanding shares of stock (voting or nonvoting) would require disregard of those shares for purposes of determining whether the parent corporation owns the requisite percentage of both voting and nonvoting stock. Clearly such an interpretation of Section 1504 is erroneous, for, contrary to the express terms of the statute, it would make qualification to file a consolidated return depend upon ownership by the parent of *less* than 80 per cent of the issued and outstanding stock. By the same token, the existence

of a dispute as to who may exercise the voting power of particular shares of stock does not require disregard of those shares in determining whether a parent corporation is qualified to file a consolidated return. The elimination of stock from the computation of the stock ownership requirements for filing a consolidated return on the basis of a dispute as to ownership or voting rights would unrealistically distort the requirements imposed by Section 1504 of the 1954 Code.[11]

Moreover, in this case to treat the 30,000 trusteed shares of Products' common stock as deprived of voting power during 1954 would be contrary to the provisions of Oregon law which control the voting rights of the stock of that corporation. With respect to the voting power of corporate stock Section 57.170 of the Oregon Revised Statutes (Appendix, *infra*) provides:

> *Voting of shares.* (1) Each outstanding share, regardless of class, shall be entitled to one vote on each matter submitted to a vote at a meeting of shareholders, except to the extent that the

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[11] For example, if a corporation owned only 10 percent of each class of the stock of a second corporation, and a dispute arose as to the ownership of the remaining 90 per cent of each class of stock, under taxpayer's theory the dominant interest should be ignored and the corporations should be qualified to file consolidated returns on the basis that the "parent's" 10 per cent interest constituted all the outstanding shares of each class of stock of the second corporation. Clearly in such a case the stock ownership requirements of Section 1504 would not be satisfied.

> voting rights of the shares of any class or classes are limited or denied by the articles of incorporation as permitted by this chapter.

Taxpayer does not contend that the voting rights of the common stock of Products are "limited or denied" by that company's articles of incorporation. Section 57.170 further states:

> (2) Neither treasury shares, nor shares of its own stock held by a corporation in a fiduciary capacity, nor shares held by another corporation if a majority of the shares entitled to vote for the election of directors of such other corporation is held by the corporation, shall be voted at any meeting or counted in determining the total number of outstanding shares at any given time.
>
> * * * *
>
> (6) * * * Shares standing in the name of a trustee may be voted by him, either in person or by proxy; but no trustee shall be entitled to vote shares held by him without a transfer of such shares into his name.

The 30,000 shares of Products' common stock held in trust during 1954 clearly were not within any of the categories of shares limited as to voting power by paragraph (2). Since those shares had been transferred into the name of the trustees (R. 28-29), under the terms of paragraph (6) the trustees were entitled to vote them. Thus Section 57.170, which is concerned with the voting rights of corporate stock and the limitations on the voting power of certain shares, imposes no limitation on the voting power of the shares in issue. Taxpayer has not indicated any

other provision of Oregon law which limits the voting power of shares owned by a voting trust in 1954. Instead, taxpayer simply alleges doubt under Oregon law as to validity of a voting trust, and asserts that because of such alleged doubt the trusteed shares were deprived of voting rights during 1954. As indicated above, the applicable Oregon statutes contain no provisions for such a limitation upon the voting power of corporate stock but on the contrary state that each share of a corporation's stock "shall be entitled to one vote on each matter submitted to a vote at a meeting of shareholders" in the absence of conditions not present in this case. In short, whether or not the voting trust was valid, the trusteed shares themselves possessed voting rights, exercisible by either the trustee or the beneficial owners.

Even in cases where the owners of corporate shares were temporarily unable to exercise their voting rights, contentions similar to those of the taxpayer properly have been rejected because the shares themselves remained voting stock.

In *Doernbecher Mfg. Co.* v. *Commissioner*, 80 F. 2d 573 (C.A. 9th), the taxpayer subsidiary claimed the privilege of filing a consolidated return under Section 141(d), Revenue Act of 1928, although the parent did not own the required 95 per cent of the voting stock of the allegedly affiliated subsidiary.[12] Tax-

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[12] The Revenue Act of 1928, c. 852, 45 Stat. 791, 831, defined "affiliated group" for consolidated return purposes as including certain chains of corporations in which—

(2) The common parent corporation owns di-

payer had entered into an agreement to purchase shares of its own stock; the stock had been placed in escrow under an agreement that the seller had no right to vote or draw dividends on the shares while in escrow; and taxpayer claimed the shares were treasury stock and should be excluded from stock to be considered in arriving at the 95 per cent ownership requirement for affiliation. This Court held, 80 F. 2d 573, that the escrowed stock "* * * was still voting stock even if the right of the seller to vote it was temporarily suspended" and that the corporations were not affiliated and might not file a consolidated return.

In *Kansas, O. & G. Ry. Co.* v. *Helvering*, 124 F. 2d 460 (C.A. 3d), after termination of a voting trust, some of the trust receipts were not turned in for stock certificates. The court held that the unclaimed voting stock for which trust receipts were not surrendered must be included in the total of the voting stock in determining whether the parent corporation had the 95 per cent ownership required for qualification to file a consolidated return.[13] The court stated (124

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rectly at least 95 per centum of the stock of at least one of the other corporations.

As used in this subsection the term "stock" does not include nonvoting stock which is limited and preferred as to dividends.

[13] The Revenue Act of 1932, c. 209, 47 Stat. 169, 213, Sec. 141(d), contains provisions identical to those of the Revenue Act of 1928 (footnote 12, *supra*) defining "affiliated group" for consolidated return purposes. The definition is unchanged in the Revenue Act of 1934, c. 277, 48 Stat. 680, 721, Sec. 141(d), except for the addition of provisions limiting the privilege to railroad corporations.

F. 2d 460, 464):

> Nor is it of any consequence that the trust receipt holders cannot vote the stock to which they are entitled until stock certificates therefor have been issued to them. The stock is voting stock none the less. It is the voting privilege with which a particular stock issue is endowed and not whether it is voted which determines its voting character within the intent of Section 141 of the Revenue Act of 1932 and 1934.

See also *Pioneer Parachute Co.* v. *Commissioner*, 6 T.C. 1246, affirmed, 162 F. 2d 249 (C.A. 2d).[14]

Taxpayer attempts (Br. 10-11) to distinguish these authorities on the ground that the 1954 Code requires

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[14] In the *Pioneer Parachute* case a subsidiary had issued shares of new non-voting preferred stock to minority shareholders in exchange for their voting stock. The new preferred stock was convertible into common stock at the shareholder's option and paid two-thirds of common stock dividends. The applicable statute, Section 730(d) of the Internal Revenue Code of 1939, as added by Sec. 201, Second Revenue Act of 1940, c. 757, 54 Stat. 974 (26 U.S.C. 1952 ed., Sec. 730) (applicable to excess profits taxes for years beginning before 1942), stated as one of the requirements for affiliation that:

> (2) The common parent corporation owns directly at least 95 per centum of each class of the stock of at least one of the other includible corporations.
>
> As used in this subsection the term "stock" does not include nonvoting stock which is limited and preferred as to dividends.

The Tax Court held that the preferred stock of the subsidiary must be treated as voting stock and that it was not entitled to join with its parent in filing a consolidated return.

for affiliation that the parent corporation own "stock possessing at least 80 percent of the voting power" whereas prior law required ownership of "at least 95 percentum of each class of stock".[15] The distinction is not valid. In fact, the statutes involved in *Dornbecher Mfg. Co.* v. *Commissioner*, *supra*, and *Kansas, O. & G. Ry. Co.* v. *Helvering*, *supra* (footnotes 12 and 13), required that the common parent own directly "at least 95 per centum of the stock" and in each case the applicable statute provides that the term "stock" does not include nonvoting preferred stock.

In *Anderson-Clayton Securities Corp.* v. *Commissioner*, 35 B.T.A. 795, the taxpayer owned 100 per cent of the preferred shares and 64 per cent of the common shares of each of six subsidiaries. The preferred stock had voting power of 50 votes per share and the common had one vote per share. The Board held this satisfied the affiliation requirement of Section 141(d) of the Revenue Act of 1928, *supra*, that the common parent own "at least 95 per centum of the stock" as the statute was concerned with ownership of "stock" rather than number of "shares". See also I.T. 3896, 1948-1 Cum. Bull. 72, to the effect that the affiliation requirements in Section 141 of the Internal Revenue Code of 1939 (and Section 1504 of the 1954 Code) in terms of "voting power" follow the *Anderson-Clayton* decision.

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[15] The latter terminology is from Section 730(d), Internal Revenue Code of 1939, *supra*, involved in the *Pioneer Parachute* case, *supra*.

Thus, even where the voting power of the owners of shares is temporarily unexercisable, the shares are considered in determining whether a taxpayer owns stock possessing sufficient voting power to satisfy the requirements for filing a consolidated return. A contrary rule would amount to an invitation to avoid the consolidated return prerequisites by the simple device of temporary suspension of voting rights of the owners of some shares.[16]

In addition, in the present case taxpayer would not qualify to file a consolidated return with Products even if, in accordance with its contentions, the 30,000 trusteed shares were not considered to have voting power in 1954. By taxpayer's own reasoning, in such case the trusteed shares would then constitute a class of nonvoting common stock. The taxpayer, as beneficial owner of 2,000 of the 30,000 shares, would not satisfy the separate requirement of Section 1504 that it own 80 per cent of such class of nonvoting stock.

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[16] See *Atlantic City Co.* v. *Commissioner,* 288 U.S. 152, 154, to the effect that Congress sought "to prevent evasion through the manipulation of intercompany transactions" in the statutes establishing affiliation requirements for the filing of consolidated returns.

CONCLUSION

The decision of the Tax Court is correct and should be affirmed.

Respectfully submitted,

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APPENDIX

Internal Revenue Code of 1954:

SEC. 1501. PRIVILEGE TO FILE CONSOLIDATED RETURNS.

An affiliated group of corporations shall, subject to the provisions of this chapter, have the privilege of making a consolidated return with respect to the income tax imposed by chapter 1 for the taxable year in lieu of separate returns. The making of a consolidated return shall be upon the condition that all corporations which at any time during the taxable year have been members of the affiliated group consent to all the consolidated return regulations prescribed under section 1502 prior to the last day prescribed by law for the filing of such return. The making of a consolidated return shall be considered as such consent. In the case of a corporation which is a member of the affiliated group for a fractional part of the year, the consolidated return shall include the income of such corporation for such part of the year as it is a member of the affiliated group.

(26 U.S.C. 1958 ed., Sec. 1501.)

SEC. 1504. DEFINITIONS.

(a) *Definition of "Affiliated Group".*—As used in this chapter, the term "affiliated group" means one or more chains of includible corporations connected through stock ownership with a common parent corporation which is an includible corporation if—

(1) Stock possessing at least 80 percent of the voting power of all classes of stock

and at least 80 percent of each class of the nonvoting stock of each of the includible corporations (except the common parent corporation) is owned directly by one or more of the other includible corporations; and

(2) The common parent corporation owns directly stock possessing at least 80 percent of the voting power of all classes of stock and at least 80 percent of each class of the nonvoting stock of at least one of the other includible corporations.

As used in this subsection, the term "stock" does not include nonvoting stock which is limited and preferred as to dividends.

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(26 U.S.C. 1958 ed., Sec. 1504.)

Oregon Revised Statutes:

Section 57.170 *Voting of shares.* (1) Each outstanding share, regardless of class, shall be entitled to one vote on each matter submitted to a vote at a meeting of shareholders, except to the extent that the voting rights of the shares of any class or classes are limited or denied by the articles of incorporation as permitted by this chapter.

(2) Neither treasury shares, nor shares of its own stock held by a corporation in a fiduciary capacity, nor shares held by another corporation if a majority of the shares entitled to vote for the election of directors of such other corporation is held by the corporation, shall be voted at any meeting or counted in determining the total number of outstanding shares at any given time.

(3) A shareholder may vote either in person or by proxy executed in writing by the shareholder or by his duly authorized attorney-in-fact. No proxy shall be valid after 11 months from the date of its execution, unless otherwise provided in the proxy.

(4) At each election for directors every shareholder entitled to vote at such election shall have the right to vote, in person or by proxy, the number of shares owned by him for as many persons as there are directors to be elected and for whose election he has a right to vote, or, if the articles of incorporation specifically permit cumulative voting, to cumulate his votes either by giving one candidate as many votes as the number of such directors multiplied by the number of his shares shall equal or by distributing such votes on the same principle among any number of such candidates.

(5) Shares standing in the name of another domestic or foreign corporation may be voted by such officer, agent or proxy as the bylaws of such corporation may prescribe, or, in the absence of such provision, as the board of directors of such corporation may determine.

(6) Shares held by an administrator, executor, guardian or conservator may be voted by him, either in person or by proxy, without a transfer of such shares into his name. Shares standing in the name of a trustee may be voted by him, either in person or by proxy; but no trustee shall be entitled to vote shares held by him without a transfer of such shares into his name.

(7) Shares standing in the name of a receiver may be voted by such receiver, and shares held

by or under control of a receiver may be voted by such receiver without the transfer thereof into his name if authority so to do be contained in an appropriate order of the court by which such receiver was appointed.

(8) A shareholder whose shares are pledged shall be entitled to vote such shares until the shares have been transferred into the name of the pledgee, and thereafter the pledgee shall be entitled to vote the shares so transferred.

Section 57.175 *Voting trust.* Any number of shareholders of a corporation may create a voting trust for the purpose of conferring upon a trustee or trustees the right to vote or otherwise represent their shares, for a period of not to exceed 10 years, by entering into a written voting trust agreement specifying the terms and conditions of the voting trust, by depositing a counterpart of the agreement with the corporation at its registered office, and by transferring their shares to such trustee or trustees for the purposes of the agreement. The counterpart of the voting trust agreement so deposited with the corporation shall be subject to the same right of examination by a shareholder of the corporation, in person or by agent or attorney, as are the books and records of the corporation, and shall be subject to examination by any holder of a beneficial interest in the voting trust, either in person or by agent or attorney, at any reasonable time for any proper purpose.

Section 57.796 *Application to corporations existing on December 31, 1953.* (1) The provisions of the Oregon Business Corporation Act shall apply to the fullest extent permitted by the

laws and Constitution of the United States and of the State of Oregon, to all existing corporations organized under any general Act of this state.

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Section 57.799 *Effect of repeal of prior Acts.* The repeal of a prior Act by chapter 549, Oregon Laws 1953, shall not affect any right accrued or established, or any liability or penalty incurred, under the provisions of such Act, prior to the repeal thereof.

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